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E.O. 12958: DECL: 06/23/2016
TAGS: TAGS
SUBJECT: SUBJECT: THE FIGHT FOR PCCW

Classified By: CLASSIFIED BY: EP Section Chief Simon Schuchat; Reasons: 1.4 (b/d)

¶1. (C) Summary: PCCW Limited (formerly known as Pacific Century CyberWorks Limited) is considering bids from three foreign suitors for its core telecommunications and media assets. Mainland Chinese telecommunications company China Network Communications Group Corporation (China Netcom), which holds a 20% stake in PCCW, subsequently stated its opposition to any changes in PCCW's assets or shareholding structures. Beyond these public statements, a reliable and well-informed source has also told us that Beijing is pulling out all the stops to keep foreigners from purchasing the PCCW assets.

¶2. (C) While there may be high level efforts to shape the sale, Hong Kong Commerce, Industry, and Technology Bureau (CITB) Principal Assistant Secretary Tony Li said that neither the Hong Kong Government (HKG) nor the mainland Chinese have a "veto" over it. He noted that a competition review was possible but would depend on the specific provisions of the final deal. Telecom industry analysts in Hong Kong pointed out that PCCW's value as a potential entry point into the mainland telecommunications and media market may already have been compromised by the negative reaction from China Netcom and possible further reactions from the mainland Chinese Government. End Summary.

PCCW "Selling Out?"

¶3. (SBU) On Tuesday, June 20, media sources indicated that a consortium led by Australian investment bank Macquarie Bank had offered to purchase PCCW Limited's telecommunications and media assets -- just the assets, rather than a share interest -- for a reported USD 7.3 billion. U.S. private equity firm Texas Pacific Group and its regionally focused subsidiary Newbridge Capital Inc. then reportedly offered a slightly higher figure. Although PCCW subsequently denied the accuracy of both reported bid figures, most industry analysts agreed that the purchase would be worth several billion dollars and that the purchase price would likely include the adoption of PCCW's 2.5 billion USD debt burden.

¶4. (SBU) On June 23, a third consortium comprised of Ashmore Investment Management, Spinnaker Capital Group, and Clearwater Capital also indicated interest in making an offer for PCCW's assets. This group had previously purchased China Netcom's undersea cable operation (Asia Netcom) for USD 402 million. PCCW refuted earlier reports that its board of directors would make a decision on the purchase bids within ten days, stating that it was under no time limit to accept or reject the purchase offers.

Opposition from China Netcom, Beijing?

¶5. (SBU) In a statement released through the Xinhua News Agency, China Netcom stated its opposition to any changes in ownership of PCCW's assets or shares because the company's assets should be, "owned and managed by Hong Kong people." China Netcom's spokesperson claimed that the company had not received any advance notice of the possible transaction and said that the sale of PCCW's assets would destabilize Hong Kong's recovering economy.

¶6. (C) Beijing's resistance to the attempted acquisitions is more than rhetorical. We have heard from a reliable and well informed source that Beijing is pulling out all the stops to keep foreigners from purchasing the PCCW assets, applying pressure behind the scenes. There may also be a Beijing-inspired effort to find Hong Kong investors to bid against the foreign interests.

¶7. (SBU) PCCW noted in a subsequent press release that it would only need to gain China Netcom's consent for transactions involving "voting interests," or shares, of the company. In transactions involving the disposal of physical assets, PCCW is only required to inform China Netcom of the transaction details before the deal is carried out. Various industry analysts noted that China Netcom has three logical courses of action left to it:

1) Dispose of its shares;

2) Take measures to block the sale; or

3) Make a counter-bid.

According to mainland telecommunications expert Lu Tingjie of the Beijing University of Posts and Telecommunications, China Netcom will have to consult with the mainland State-owned Assets Supervision and Administration Commission (Sasac) before taking any action related to the PCCW situation.

HKG Comments

¶8. (C) CITB Principal Assistant Secretary Tony Li told us that the HKG and the mainland Chinese government do not have any way to "veto" the purchase of PCCW's assets by a foreign company. Li said that the HKG does not object to foreign ownership of telecommunication infrastructure; for example, Hong Kong based CSL Mobile is completely owned by Australian telecommunications firm Telstra. In any case, it would be inappropriate for Hong Kong regulators to be swayed by political considerations, even if they come from Beijing. Li concluded that Beijing disapproval of the situation could only affect the PCCW sale in a political sense, perhaps by implying a difficult road for any future mainland business projects attempted by both PCCW Chairman Richard Li and his father, Li Ka-Shing.

¶9. (C) Depending on how the PCCW deal is structured, however, the HKG could conduct a competition review of the deal. The Office of the Telecommunications Authority (OFTA) has the power to block mergers and acquisition if the actions involve changes in carrier licenses and are judged to have a substantially adverse affect on competition in the telecommunications sector.

Telecom Analysts React

¶10. (C) Credit Suisse Telecom analyst Jeffrey Tan speculated that the high caliber of the potential buyers would continue to draw greater interest and predicted that more potential

suitors for PCCW would emerge. Their primary interest is gaining entry into the nascent Chinese integrated internet services/media market, an area in which PCCW holds a high level of expertise. Tan said that one possible way to overcome resistance from China Netcom and the mainland Chinese government would be for foreign entities to entice China Netcom to join in on the purchase. They could also bring in yet another operator, such as Singtel, that would be more politically acceptable to the mainland authorities. In any case, continued Tan, Richard Li has much to gain if share values for PCCW rise in reaction to the speculation. Li might even be working with his friends to bid up the share prices, although such a move would be like "playing with fire" and could even affect his father's business interests, said Tan.

¶11. (C) Hong Kong University Telecommunications Research Project (TRP) Director John Ure commented that Hong Kong's telecom market is saturated and offers little potential for future growth, so PCCW's real value to purchasers is its link with China and its ability to leverage its Cable TV service based on broadband internet connections (Broadband TV), a concept that is practically unique to Hong Kong at this stage. Ure said that PCCW's Broadband TV offerings are its "crown jewel," and observed that PCCW's Broadband TV specialist Paul Berryman is in great demand as a consultant to media companies in the region. Ure opined that Richard Li has wanted to extricate himself from the telecommunications business for quite some time and return to his "roots" as a property developer. If PCCW successfully sells all of its telecommunications and media assets, the company would once again be a property/real estate company - this time, though, with a great deal of cash with which to pursue other ventures.

COMMENT

¶12. (C) Comment: For Beijing, this possible deal is a matter of national security involving key strategic infrastructure in Hong Kong. For Hong Kong, this single deal would be equivalent to approximately 20% of the total foreign direct investment in the territory in 2005 and a symbol of Hong Kong's openness to international business, a feature of the city that the HKG tirelessly promotes. Hong Kong independent legislator Albert Cheng also stated that any overt attempt to stop foreign investors buying the assets could hurt the

territory's image as an open city for international investment. No matter what happens, it seems likely that the final result will have consequences for security and sovereignty issues in Hong Kong. End Comment.
Cunningham